

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)
)
Petition of Qwest Corporation for) WC Docket No. 07-204
Forbearance from Enforcement of the)
Commission’s ARMIS and 492A)
Reporting Requirements Pursuant to 47)
U.S.C. § 160)

REPLY COMMENTS OF VERIZON¹

Introduction and Summary

More than six years ago the Commission concluded that the right question was not *whether* historical reporting obligations such as the ARMIS reports should be eliminated – “but rather *when*.”² Since the *Phase Two Order* the remaining BOCs have lost more than 20 percent of their lines³ and intermodal competition has exploded. The time to eliminate the ARMIS reports is now. The Commission should do away with ARMIS reporting for all providers.

¹ The Verizon companies participating in this filing (“Verizon”) are the regulated, wholly owned subsidiaries of Verizon Communications Inc.

² *2000 Biennial Regulatory Review – Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers: Phase 2 Amendments to the Uniform System of Accounts for Interconnection Jurisdictional Separations Reform and Referral to the Federal-State Joint Board Local Competition and Broadband Reporting*, Report and Order and Further Notice of Proposed Rulemaking, 16 FCC Rcd 19911, ¶ 206 (2001) (“*Phase Two Order*”) (emphasis added).

³ Compare SBC, *Investor Briefing* at 16 (Jan. 28, 2003) and BellSouth, *4Q 2002 Results* at 9 (Jan. 23, 2003) with AT&T Inc., *Investor Briefing: 3rd Quarter 2007* at 21 (Oct. 23, 2007) (http://www.att.com/Investor/Financial/Earning_Info/docs/3Q_07_IB_FINAL.pdf); compare Verizon, *Investor Quarterly 4Q 2002* at 13 (Jan. 29, 2003) with Verizon, *Investor Quarterly Q3 2007* at 17 (Oct. 29, 2007) (<http://investor.verizon.com/financial/quarterly/vz/3Q2007/3Q07Bulletin.pdf>); compare Qwest Press Release, *Qwest Communications Reports Fourth Quarter and Full-Year 2002 Unaudited Results and Fourth Quarter Financials*, Attachment E (Feb. 19, 2003) (

I. The Purpose Of The ARMIS Reports Is No Longer Valid Under Price Cap Regulation And A Robustly Competitive Market.

There are generally three varieties of ARMIS reports⁴ – financial reports, service quality reports, and infrastructure reports. The Commission adopted the original ARMIS financial reports more than 20 years ago to “facilitate the timely and efficient analysis of revenue requirements and rates of return. . . .”⁵ Other ARMIS financial reports were adopted because “forecasts of relative use were identified . . . as key elements in the accurate allocation of costs on a cost causal basis because many costs are incurred in anticipation of future demand rather than in response to the current level and pattern of demand for service.” *ARMIS Order* ¶ 45.

The ARMIS financial reports primarily contain cost data that relates only to rate of return regulation. Even after moving to price cap regulation in the 1990s, the Commission preserved the ARMIS financial reports in order to monitor the transition to price caps and to compile financial data sufficient to conduct a subsequent review of its then-new regulatory regime.⁶ The Commission also added the ARMIS service quality and infrastructure reports in order to: (1) respond to concerns about the transition to price cap regulation; (2) accumulate data in order to

ir.net/phoenix.zhtml?c=119535&p=irol-reportsOther) with Qwest Press Release, *Qwest Announces Third Quarter 2007 Results – Continued Progress in Revenue, Cash Flow and Margin Trends and Third Quarter Financials*, Attachment D (Oct. 30, 2007) (<http://phx.corporate-ir.net/phoenix.zhtml?c=119535&p=irol-reportsAnnual>).

⁴ Qwest also seeks forbearance from FCC Report 492A, a rate of return report still required of price cap carriers. Under price cap regulation, Report 492A and the rate of return rules in Subparts D and E of the Commission's rules have nothing to do with rates charged by price cap carriers. There is no reason for the Commission to retain these rules or this report for price cap carriers.

⁵ *Automated Reporting Requirements for Certain Class A and Tier 1 Telephone Companies (Parts 31, 43, 67, and 69 of the FCC's Rules)*, Report and Order, 2 FCC Rcd 5770, ¶ 1 (1987) (“*ARMIS Order*”).

⁶ *Policy and Rules Concerning Rates for Dominant Carriers*, Order on Reconsideration, 6 FCC Rcd 2637, ¶ 198 (1991) (“*Carrier Rate Order*”).

facilitate the Commission's review of the price cap regime; and (3) out of "an abundance of caution." *Carrier Rate Order* ¶ 179.

Under price cap regulation, now itself more than 15 years old, the cost information in the ARMIS financial reports is irrelevant. Price caps are cost agnostic. And in today's environment, even if the Commission were to make adjustments to its price cap regime those changes must foremost be driven by the competitive landscape and not a regressive analysis of carrier costs as Sprint suggests.⁷ In that context, commenters generally do not dispute – nor could they – that the original purpose of the ARMIS financial reports has vanished. Moreover, the vibrant competition of the last several years has washed away any remaining justification for even the ARMIS service quality and infrastructure reports. These reports were adopted as temporary mechanisms to ensure that price cap regulation functioned properly. They were arguably unnecessary from the start and are especially inappropriate now as customers seeking voice service have a host of competitive choices, including cable companies, wireless carriers, and VoIP providers.

Cable companies have been particularly successful competitors and collectively are expected to serve more than 13 million voice lines by the end of this year and more than 19 million lines by year-end 2008.⁸ Cable companies provide voice service on a near ubiquitous basis over their own networks and are expected to offer telephony service (IP-based or circuit-

⁷ Comments of Sprint Nextel Corporation ("Sprint Comments") at 4.

⁸ Craig Moffett, *et al.*, Bernstein Research, *VoIP: The End of the Beginning*, at Ex. 8 (April 3, 2007).

switched) to some 95 percent of households by the end of this year and to 99 percent of U.S. households by the end of 2008.⁹

For example, Comcast currently markets voice telephone service to 40 million homes, which represents 83 percent of its cable footprint. As of September 30, 2007, Comcast had approximately 3.8 million voice telephone customers and its phone revenues increased 91 percent to \$1.2 billion from \$652 million in 2006.¹⁰ Likewise, Time Warner Cable had more than 2.6 million voice telephone customers as of September 2007, which represents an 11 percent penetration of service-ready homes passed, and it added 275,000 digital voice customers during the third quarter of 2007, marking its largest quarterly gain ever.¹¹ Cox provides voice telephone service to more than 2.1 million residential customers and 160,000 businesses.¹² Charter currently provides telephone service to more than 800,000 customers, more than double the number of customers it served as of September 2006, and Charter expects its telephone service to reach approximately 10 million homes passed by the end of 2008.¹³

Wireless companies also are successfully offering competing telephony service. According to the Commission's most recent wireless report, 98 percent of the total U.S.

⁹ *Id.* at Ex. 3.

¹⁰ Press Release, "Comcast Reports Third Quarter 2007 Results" (Oct. 25, 2007) (http://media.corporate-ir.net/media_files/irol/11/118591/Earnings_3Q07/release_pdf.pdf).

¹¹ News Release, "Time Warner Cable Reports Third Quarter 2007 Results" (Nov. 7, 2007) (http://files.shareholder.com/downloads/TWC/176374502x0x142004/f93e9bb7-2f1c-4d32-bc01-50e5b44fdfdb/FINAL_TWC%203Q07%20PR_110607.pdf).

¹² News Release, "Cox Communications Receives J.D. Power and Associates' Highest Honor in Residential Telephone Satisfaction in Three Regions" (July 11, 2007) (<http://phx.corporate-ir.net/phoenix.zhtml?c=76341&p=irol-newsArticle&t=Regular&id=1024989&>).

¹³ Press Release, "Charter Reports Third-Quarter Financial and Operating Results" (Nov. 7, 2007) (<http://phx.corporate-ir.net/phoenix.zhtml?c=112298&p=irol-newsArticle&ID=1074737&highlight=>).

population already has access to three or more different wireless providers in the counties where they live.¹⁴ Wireless handsets are rapidly displacing landline telephones. Approximately 16 percent of all households are projected to be wireless-only by the end of this year, and the number of wireless-only households is expected to increase steadily over the next five years.¹⁵ By 2012, nearly one-third of all households are projected to have at least one cellphone but no landline telephone. *Id.*

Independent VoIP providers also are aggressively marketing their services and competing for voice customers.¹⁶ In an effort to entice customers to purchase its VoIP service, Via Talk, for example, is offering new customers “two unlimited phone lines for the price of one” in addition to a “match in the form of a service credit, up to 3 months of free service for any prepaid contracts [a customer] ha[s] with any other phone service provider, for service switched to [its] network.”¹⁷

¹⁴ See *Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services*, Eleventh Report, 21 FCC Rcd 10947, ¶ 41 (Sept. 29, 2006) (proceeding terminated). According to the same report, “94 percent of the U.S. population, live[s] in counties with four or more mobile telephone operators competing to offer service . . . 51 percent of the U.S. population, live[s] in counties with five or more mobile telephone operators competing to offer service, [and] 18 percent of the population, live[s] in counties with six or more mobile telephone operators competing to offer service.” *Id.*

¹⁵ See Letter from Evan T. Leo, counsel for Verizon, to Marlene H. Dortch, FCC, *Petitions of the Verizon Telephone Companies for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Boston, New York, Philadelphia, Pittsburgh, Providence and Virginia Beach Metropolitan Statistical Areas*, WC Docket No. 06-172 at 7 (Nov. 16, 2007), citing and attaching as Attachment C, S. Flannery, *et al.*, Morgan Stanley, *Cutting the Cord: Wireless Substitution Is Accelerating* at 3, Exhibit 2 (Sept. 27, 2007).

¹⁶ See, e.g., Jason Armstrong, *et al.*, Goldman Sachs, *2007 Telecom Outlook: Sector Not Cheap, But Opportunities Abound*, at Ex. 14 (Feb. 6, 2007) (estimating that cable and stand-alone VoIP will serve more than 20% of voice access lines by end-of-year 2010).

¹⁷ See http://www.viatalk.com/internet_phone_special.htm (last visited Dec. 19, 2007).

Contrary to the claims of the NASUCA Commenters, in such a competitive environment it is customer choice that drives service quality and infrastructure upgrades, not arcane regulatory reporting requirements applicable to only a few among many competitors.¹⁸ Indeed, even if the ARMIS reporting process added material consumer value in a competitive market, which it does not, any potential value is lost in the application of the reporting requirements themselves. The requirements apply only to a small subset of ILECs, and in some cases only to AT&T, Verizon, and Qwest. Competitive LECs, cable companies, wireless carriers, and independent VoIP providers are not subject to *any* ARMIS reporting requirements. Consumers could not possibly make informed competitive choices by analyzing narrow categories of data from only a few among many competitors. To that end, Chairman Martin gets it exactly right: “Market forces and competition are better drivers of innovation and better protectors of consumer interest. Competition – not regulation – best leads to better services and lower prices.”¹⁹

Only the NASUCA Commenters even attempt to address the transformation of the communications marketplace since price cap regulation and adoption of the ARMIS reports. They argue that because ILECs retain a substantial share of the market for “basic local telephone service” provided over switched access lines, the ARMIS reports must be retained. NASUCA Comments at 31. This misses the point entirely. It is only by narrowly defining the relevant market do the NASUCA Commenters attempt to justify continued regulation, and even with that

¹⁸ Joint Comments and Opposition of the New Jersey Division of Rate Counsel, the Public Counsel Section of the Washington State Attorney General’s Office, and the National Association of State Utility Consumer Advocates (collectively “NASUCA Commenters”)(“NASUCA Comments”) at 37.

¹⁹ Remarks of Chairman Kevin J. Martin, Georgetown University McDonough School of Business’s Center for Business and Public Policy, http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-268774A1.pdf (Nov. 30, 2006).

definition their justification falls flat. While it is true that in certain instances ILECs remain providers of choice for customers that desire traditional basic local telephone service, most modern telecommunications consumers demand much more than POTS. They want the next generation telecommunications services offered by a variety of providers using a variety of technologies. The NASUCA Commenters blindly dismiss all intermodal competition and customer choice incentives out of hand by concluding with zero factual support that while available, intermodal alternatives “do not provide economic substitutes for basic local service.” *Id.* This is simply wrong, and the same competition that the NASUCA Commenters ignore is what should compel the Commission to eliminate the ARMIS reports.

II. The Desire Of Competitors To Use ARMIS Data To Challenge The Reasonableness Of Special Access Prices Is Improper And Misguided.

Some commenters support retaining the ARMIS reports because of the tired claim that ARMIS financial data is needed to attack special access returns in other, unrelated proceedings.²⁰ As Verizon and other carriers have repeatedly explained, these segment-specific ARMIS data are *not* accurate reflections of a carrier’s actual returns, but rather are artifacts of the Commission’s rules for allocating network investment among services. The need to allocate shared and common costs in the ARMIS financial reports means that this process will inevitably yield

²⁰ Comments of AdHoc Telecommunications Users Committee (“AdHoc Comments”) at 7; Sprint Comments at 15; NASUCA Comments at 38. AdHoc’s opposition to ARMIS forbearance is more generally puzzling. AdHoc claims that its interests are actually “served by avoiding imposition of unnecessary regulatory constraints on incumbent service providers” and that in “an effectively competitive market, AdHoc’s members do not need regulation to protect their interests and would not advocate it.” AdHoc Comments at FN 1.

arbitrary results. The Commission has been clear on this point: The accounting rates of return reported in ARMIS do “not serve a ratemaking purpose.”²¹

Indeed, ARMIS reports themselves do not even provide rates of return – they merely provide cost and revenue data that some parties have used to try to calculate returns. ARMIS data suffer from shortcomings that make them unreliable both for analyzing returns in any given year, and for comparing annual returns over time.²² The ARMIS accounting categories for special access do not track the economic costs for these services, but are driven instead by artificial regulatory considerations such as jurisdictional separations and divisions between regulated and unregulated services. Taylor Supp. Decl. ¶ 44. Relatedly, the ARMIS cost categories were subject to a separations freeze in June 2001 that distorts any attempt to use these data to approximate special access rates of return.²³ The freeze was implemented “to provide stability and simplification for the separations process pending comprehensive reform.” *Id.* ¶ 10. Having determined that it made no sense to make carriers endure the “regulatory burden” of recalibrating their cost allocations “during the transition from a regulated monopoly to a deregulated, competitive environment in the local telecommunications marketplace,” *Id.* ¶ 13, it would be arbitrary and capricious for the Commission to rely on those frozen categories as a proxy for the costs of providing special access that carriers incur today.

²¹ *Policy & Rules Concerning Rates for Dominant Carriers*, Order on Reconsideration, 6 FCC Rcd 2637, ¶ 199 (1991).

²² See Comments of Verizon, *In the Matter of Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25 & RM-10593 (Aug. 8, 2007) at 43, citing Attachment A, Supplemental Declaration of Dr. William E. Taylor on Behalf of Verizon (“Taylor Supp. Decl.”) (April 8, 2007).

²³ See *Jurisdictional Separations and Referral to the Federal-State Joint Board*, Report and Order, 16 FCC Rcd 11382 (2001).

ARMIS is simply not a useful tool in the special access context, either for measuring absolute special access rates of return in a given year or for assessing trends in such returns from year to year. Taylor Supp. Decl.¶ 44.

III. State Use Of ARMIS Data Is Not A Legitimate Reason To Retain The Federal Reporting Requirements.

Commenters focus much of their opposition to eliminating the ARMIS reports on various alleged uses of the reports by state regulators.²⁴ As a threshold matter, the remaining BOCs already operate under price cap regulation – or deregulation – in most of their states, and the clear state trend is toward price caps and ultimately deregulation. The ARMIS reports are just as irrelevant in price cap and deregulated states as they are in the federal price cap context. In addition, the same robust competition that is occurring nationwide is a far better service quality and infrastructure upgrade incentive than arcane reporting requirements – regardless of the state regulatory regime

State commission commenters also argue that ARMIS data is useful in helping them analyze state-specific and national trends among carriers. *See, e.g.*, Washington UTC Comments at 3. The Act, however, does not give the Commission authority to serve as data-gatherer for the states – and the Commission cannot continue to mandate burdensome and unnecessary requirements that apply to only a few among many competitors in order to advance state regulatory functions.

²⁴ *See* Comments of the California Public Utilities Commission and the People of the State of California at 3; Comments of the Colorado Public Utilities Commission at 4; Comments of the Washington Utilities and Transportation Commission (“Washington UTC Comments”) at 2; NASUCA Comments at 9; Sprint Comments at 14.

IV. Forbearance Is The Proper Tool To Eliminate The ARMIS Reports.

Sprint asserts and other commenters imply that the forbearance process is an inappropriate venue for the Commission to consider eliminating the ARMIS reports. *See, e.g.*, Sprint Comments at 3. Sprint even goes so far as to recommend that rather than eliminate the ARMIS reports the Commission should convene a new federal-state joint board to consider changes to the ARMIS reporting process. Sprint Comments at 6. This argument misses the point. The ARMIS process does not need to be fine-tuned; it is unnecessary in today's competitive environment and needs to be eliminated. Further, Sprint's true motivation to see that its competitors remain hamstrung by burdensome and outdated regulatory obligations is self-evident now that Sprint has spun off its ILEC operations, and is therefore free of ARMIS reporting requirements.

Section 10 forbearance was designed precisely for situations such as this – where antiquated regulatory requirements are no longer necessary to ensure reasonable rates or to protect consumers. 47 U.S.C. § 160. Indeed, elimination of outdated and unnecessary regulations such as the ARMIS reports is required to ensure that the pro-competitive, deregulatory goals of the Act are realized.²⁵ The Act itself embodies the principle that unnecessary and inefficient rules and requirements should be eliminated. In fact, Congress

²⁵ *See, e.g., AT&T v. FCC*, 452 F3d 830, 832 (D.C. Cir. 2006) (“Critical to Congress’s deregulation strategy, the [1996] Act added section 10 to the Communications Act of 1934”); *2000 Biennial Regulatory Review*, Notice of Proposed Rulemaking, 15 FCC Rcd 20008, ¶ 1 (2000) (“The major purpose of the 1996 Act is to establish ‘a pro-competitive, deregulatory national policy framework’ designed to make available to all Americans advanced telecommunications and information technologies and services ‘by opening all telecommunications markets to competition.’ Congress empowered the Commission with an important tool to realize this goal in Section 10 of the Act.”) (citations omitted).

expressly directed that the Commission eliminate outdated and unnecessary telecommunications regulations that are no longer in the public interest.²⁶

Moreover, granting forbearance from the ARMIS reporting obligations would not affect the consumer safeguards put in place by the Commission's recent *Non-Dominant Order*²⁷ as AdHoc and Sprint suggest.²⁸ In the *Non-Dominant Order* the Commission established "imputation requirements to help monitor BOC provisioning of [access] services for possible price discrimination" *Id.* ¶ 95. In order "[t]o facilitate the transparency of each carrier's imputation of in-region, long distance costs," the Commission indicated that the BOCs should reflect the imputation charges in their ARMIS filings, "accompanied by an explanatory footnote for each line item identifying the amount imputed." *Id.* ¶ 104. The Commission further pointed to ARMIS filings as the repository of information concerning the imputation amounts – but that direction presumed the status quo ARMIS filing obligations. Even with that obligation removed, those carriers subject to ARMIS reporting would still be required to maintain records concerning the amounts imputed or charged consistent with the *Non-Dominant Order* itself and myriad other accounting safeguards such as Securities and Exchange Commission requirements, Generally Accepted Accounting Principles obligations, the Foreign Corrupt Practices Act, and the Sarbanes-Oxley Act.

²⁶ See 47 U.S.C. § 161 (mandating that the Commission review all of its regulations relating to providers of telecommunications service and "determine whether any such regulation is no longer necessary in the public interest as the result of meaningful economic competition between providers of such service," in which case the Commission "shall repeal or modify" the subject regulation).

²⁷ Section 272(f)(1) *Sunset of the BOC Separate Affiliate and Related Requirements*, Report and Order and Memorandum Opinion and Order, 22 FCC Rcd 16440, ¶ 27 (Aug. 31, 2007) ("*Non-Dominant Order*").

²⁸ AdHoc Comments at 5; Sprint Comments at 8.

Given the transition to federal price cap regulation, completed long ago, and the huge surge in intermodal competition since the Commission concluded that the ARMIS reports should be eliminated in the *Phase Two Order*, it is difficult to imagine a regulatory scheme more ripe for forbearance than the ARMIS reports.

Conclusion

The Commission should eliminate ARMIS reporting for all providers.

Respectfully submitted,

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